

Benefit Computation and Automatic Adjustment Provisions

The primary insurance amount (PIA) is the monthly benefit amount payable to the worker upon retirement at age 65 or upon entitlement to disability benefits. The PIA is also the base figure from which monthly benefit amounts payable to the worker's family members or survivors are determined. The PIA is derived from the worker's annual taxable earnings, averaged over a time period that encompasses most of the worker's adult years. Until the late 1970s, the average monthly wage (AMW) was the earnings measure generally used. For worker's first eligible for benefits in or after 1979, average indexed monthly earnings (AIME) have replaced the AMW as the usually applicable earnings measure. The PIA computation based on AIME currently involves the following three steps:

- Indexing of earnings. The worker's annual taxable earnings after 1950 are updated, or indexed, to reflect the general earnings level in the indexing year—the second calendar year before the year in which the worker is first eligible, that is, first reaches age 62, becomes disabled, or dies. Earnings in years after the indexing year are not indexed but instead are counted at their nominal value. A worker's earnings for a given year are indexed by multiplying them by the following ratio (indexing factor): The average wage in the national economy for the indexing year, divided by the corresponding average wage figure for the year to be indexed. Table 2.A8 shows the indexing factors applicable to the earnings of workers who were first eligible in 1986–99. Table 2.A9 shows indexed earnings for workers first eligible in 1992–99 who had maximum taxable earnings in each year after 1950.

- Determining AIME. The length of the computation period used in calculating AIME equals the number of full calendar years elapsing after age 21, or 1950 if later, and up to the year of first eligibility, less generally 5 dropout years. (For workers who become disabled before age 47, the number of dropout years varies from 0 to 4 depending on the worker's age and child care dropout years—see “1980 Act” in table 2.A10.) The minimum length of the computation period is two years. The actual years selected for the computation period—the computation years—are the years of highest indexed earnings after 1950, including any years before age 22 or after age 61 as well as the year of disability or death. AIME are calculated as the sum of indexed earnings in the computation period, divided by the number of months in that period. Table 2.A10 outlines the history of provisions relating to the determination of AIME and AMW.

- Computing the PIA. The formula used to compute the PIA from AIME is weighted to provide a higher ratio of benefit to AIME for workers with comparatively lower AIME. The formula applies declining conversion rates to three AIME brackets. For workers who reach age 62, become disabled, or die in 1998, the formula provides a PIA equal to:

90 percent of the first \$505
of AIME, plus
32 percent of the next
\$2,538 of AIME, plus
15 percent of AIME
over \$3,043.

Beginning with the first year of eligibility, the PIA is increased by cost-of-living adjustments (COLAs). Table 2.A11 shows the PIA formula and first applicable COLA for workers first eligible in 1979 or later.

The dollar amounts defining the AIME brackets are referred to as bend points. These bend points—see table 2.A11—are updated automatically each year in proportion to increases in the national average wage level to ensure that benefit levels for successive annual cohorts of newly eligible workers keep up with rising earnings levels and thus incorporate constant rates of earnings replacement.

The benefit formula applicable to a worker depends on the year of first eligibility rather than, for example, on the year of retirement. Thus the PIA of a worker retiring at age 65 in 1999 is calculated using the benefit formula that applies to all workers first eligible in 1996. The PIA derived from that formula is then increased by the COLAs effective for December 1996, 1997, and 1998 to obtain the PIA effective at age 65. Analogously, when a worker's benefit is recomputed based on earnings recorded after the original benefit computation, the benefit formula used in that earlier computation is applied to the recalculated AIME and the resulting PIA increased by all COLAs beginning with the one effective for the year of first eligibility to establish the new PIA.

Workers with low earnings but steady attachment to the workforce over most of their adult years may qualify for monthly benefits based on the special minimum PIA computation. This computation—described in table 2.A12—does not depend on the worker's average earnings but on the number of coverage years—years in which the worker had earnings equal to or above a specified amount. The level of the special minimum PIA is the same for workers with the same number of coverage years, irrespective of age or year of first eligibility. Increases in the special minimum PIA are linked to COLAs.

The monthly benefits payable to the worker and family members or to the worker's survivors are subject to a maximum family benefit amount. The maximum benefit for retired-worker families or survivor families—see table 2.A13—varies, by PIA level, between 150

and 188 percent of the PIA. The bend points defining the PIA brackets in this formula are automatically adjusted in proportion to increases in the national average annual wage. The maximum benefit for disabled-worker families—see table 2.A14—is the smaller of 85 percent of AIME (or 100 percent of PIA if larger) and 150 percent of the PIA.

Like the formula for determining the PIA, the maximum family benefit formula applicable to a worker depends on the year of first eligibility. Once the worker's maximum family benefit amount for the year of first eligibility is determined, it is updated in line with the COLAs.

Tables 2.A15 And 2.A16 describe benefit computations based on the worker's nonindexed earnings after 1936 and 1950, respectively. Very few persons currently being awarded benefits have PIA's computed under these old-start or new-start computation methods. These methods, particularly the new-start method shown in table 2.A16, are more frequently applicable in earnings recomputations for workers who reached age 62 before 1979. Table 2.A17 shows the maximum family benefit amounts applicable in cases of first eligibility before 1979.

The following tabulation shows the history of provisions concerning the rounding of benefit amounts.

Act	Type of rounding
1935	Nearest cent.
1950	Next higher \$.10 at each computation step.
1981	Next lower \$.10 at each computation step. Final individual benefit check (after the Supplemental Medical Insurance [SMI] premium for Part B of Medicare and some other deductions, if any) to next lower \$1 (if not already multiple of \$1).

A cost-of-living increase in benefits generally is established each year if the Consumer Price Index for Urban

Wage Earners and Clerical Workers (CPI-W), prepared by the Department of Labor, indicates a percentage increase after rounding of at least 0.1 percent between two specified quarters. The arithmetical mean of the CPI-W for July, August, and September in the year of determination is compared with the arithmetical mean of the CPI-W for the later of (a) July, August, and September in the year in which the last effective cost-of-living increase was established or (b) the 3 months of the calendar quarter in which the effective month of the last general benefit increase occurred. The percentage increase in the CPI-W, rounded to the nearest 0.1 percent, represents the size of the increase in benefits, effective for December of the year in which the determination is made.

Under certain conditions, depending on the size of the combined OASDI Trust Funds relative to estimated disbursements, the applicability and size of a cost-of-living adjustment are determined under an alternative method, called the stabilizer provision. In no case, however, are benefits reduced below the level of benefits in the year of determination. The history of the provisions relating to the automatic adjustment of benefits, including a description of the stabilizer provision, is presented in table 2.A18.

In addition, table 2.A18 includes a summary history and description of provisions relating to the annual automatic adjustment of (1) the maximum amount of taxable and creditable earnings; (2) the dollar amount needed to establish a quarter of coverage; (3) the bend points defining the AIME brackets in the PIA formula and the PIA brackets in the maximum family benefit formula; and (4) the exempt amounts under the earnings (retirement) test. All of these adjustments are linked to increases in the national level of the average annual wage rather than in the CPI.

Table 2.A19 illustrates the cumulative effect of statutory and automatic increases in benefits for workers who have been in benefit status over varying time periods.